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GOALS AND RULES FOR FARM TENANCY IMPROVEMENT

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I. Introduction

The history of American farm tenure has been a continual struggle to achieve farm ownership. While ownership is desired because it represents wealth and given status there can be little doubt that it is also desired because it provides fixity of security of tenure, freedom of operation, and freedom of improvement -- the three F's of farm tenure improvement.^{1/} Briefly, freedom of production has been a major tenure goal. If this goal is rational then it should be consistent with the private free enterprise economy in which it arose. Yet recent efforts to deduce a model of the perfect lease from the model of the perfectly competitive economic system suggested that the appropriate goal towards which economists in farm tenure should direct their efforts is economic efficiency. What, then, should be the goal of tenure improvement efforts? What is the nature of the imperfection in share rent leases? Can it be removed? What rules can be followed to create a more perfect lease? The purpose of this article is to answer these questions. Left aside are many important questions of the firm such as land values, rental rates, size of units and capital requirements.

The emphasis on efficiency as a tenure goal apparently got its start when Schickele made a study of the effect of tenure systems on agricultural efficiency in 1941. He believed that security of tenure, freedom of improvement, and freedom of operation affected the farmer's efficiency. As a result he concluded that owner operation was more efficient than cash leasing because owner operators had more security and more freedom. He also concluded that share rent leasing was less efficient than either cash rent leasing and owner-operatorship primarily because the tenant paid all of the operating costs but received only a share of the product.^{2/}

^{1/} William G. Murray, Agricultural Finance, Iowa State College Press Ames, 1947, ch. 30. See also the Report of the President's Committee, Farm Tenancy, U. S. Government Printing Office Washington, 1937, which stresses the need for greater security and freedom to improve.

^{2/} Rainer Schickele, "Effect of Tenure Systems on Agricultural Efficiency," Journal of Farm Economics, Vol. 23, No. 1, February 1941, p. 194, 197. This criticism of share rent leases has a long history. It was debated by the French Physiocrats; Adam Smith, John Stuart Mill, and Alfred Marshall among others. For an excellent review see D. Gale Johnson, "Resource Allocation Under Share Contracts," Journal of Political Economy, Vol. 58, No. 2, April 1950, pp. 111-114. Schickele's contributions was that he was apparently first to recognize that if the landlord shared the costs, the problem was mitigated.

Heady agreed with Schickele that share rent leases were inefficient but concluded that "Unfavorable comparison between farm ownership and tenancy has often resulted because analysis has stopped with the isolation of imperfect leasing customs. Yet in theory perfect leasing systems are possible."^{3/} He declared that a perfect leasing system is one which ". . . must thus result in (1) the most efficient organization of resources on a farm relative to consumer demand as expressed in market prices, and (2) an equitable division of the product among the owners of the various resources employed in production."^{4/} Heady's arguments to achieve the perfect share rent lease (or efficiency) have been reduced to four rules. These rules are:

- (1) The arrangements for sharing costs and production for each particular crop must be the same.
- (2) The shares of all competitive crops must be the same.
- (3) A specific rental must be paid for each kind of resource leased that is equal to its contribution to production.
- (4) The tenant must be given prospects for return over time comparable to those of owner operators by either a long term lease or by compensating the tenant for the unexhausted value of his improvements when the lease is terminated.^{5/}

^{3/} Earl O. Heady, "Economics of Farm Leasing Systems," Journal of Farm Economics, Vol. 29, No. 3, August 1947, p. 678.

^{4/} Heady, "Economics of Farm Leasing Systems", p. 660. The same statement regarding perfect leasing is found in his Economics of Agricultural Production and Resource Use, Prentice Hall, Inc., New York, 1952, p. 589.

^{5/} Heady's requirements for a perfect share rent lease can be found in either his journal article or his textbook cited in footnote 3 above. However, they were first reduced to "incentive conditions" or rules by Virgil L. Hurlburt, Farm Rental Practices and Problems in the Midwest, North Central Regional Publication 50, Iowa Agricultural Experiment Station, Research Bulletin 416, 1954, p. 86-91. For Heady's statement of these rules see his Marginal Productivity of Resources and Imputations of Shares for Cash and Share Rented Farms, Iowa Agricultural Research Bulletin 433, 1955, p. 601.

D. Gale Johnson took Heady's emphasis on efficiency at face value but produced evidence that share rent leases were probably as efficient as cash leases.^{6/} He also found fault with Heady's first and last rules. While he recognized that sharing the costs as the product is shared permits a more rational allocation of resources he agrees with Schickele when he states that " . . . within the framework of the crop share lease the possibility of sharing costs is limited in scope. The most complete sharing is in the livestock-share lease but this involves a fairly radical departure from the crop-share basis." An alternative would be for the landlord to specify in the lease how the farming should be done. But he concludes that "It seems unlikely that either of the alternatives discussed is sufficient to prevent the tenant from 'exploiting' the landlord. In my opinion this restraint is the short-term lease. This type of lease is allged to be a serious shortcoming of American tenure institutions; but without it there seems little likelihood that the crop share lease would lead to reasonably efficient use of land."^{7/}

While Heady has not replied directly to this criticism he states that, "Given other imperfection which exist in leasing systems, the short spans of the lease may also make positive contributions to resource efficiency farming intensity may be extended to a level paralleling that of owner operation However, the perfect lease is far from being attained when the imperfections inherent in short term leases are used as a positive mechanism for offsetting more serious leasing limitations."^{8/}

^{6/} D. Gale Johnson, "Resource Allocation Under Share Contracts," Journal of Political Economy, Vol. 58, No. 2, April 1950, p. 118. Three empirical studies made since 1950 support Johnson's contentions. These are: Earl O. Heady and Earl W. Kehrberg, Relationship of Crop-Share and Cash Leasing System to Farming Efficiency, Iowa Agricultural Experiment Station Research Bulletin 386, 1952, and Walter G. Miller, Walter E. Chryst and Howard W. Ottoson, Relative Efficiencies of Farm Tenure Classes in Intrafarm Resource Allocation. (North Central Regional Publication No. 84.) Iowa Agricultural Experiment Station Research Bulletin 461, 1958, and an unpublished study of the Scully Estate, Economics Department, South Dakota Agricultural Experiment Station, 1955. In the Scully Estate study no significant differences in crops grown, livestock produced, or practices used was found between owner-operators, share tenants, and one-year cash tenants of the Scully Estate. The Scully Estate tenants were required to grow more legumes but even this did not effect their other practices nor the amount of livestock to a significant degree.

^{7/} Johnson, p. 119

^{8/} Heady, Economics of Agricultural Production and Resource Use, p. 616.

This last statement suggests that while efficiency may be a necessary condition for a perfect lease it is not a sufficient condition. What is the theoretically perfect lease? Despite the adoption by many tenure workers of conditions and rules designed to make the share rent lease more nearly perfect, the "perfect lease" does not appear to have been clearly defined. A hypothesis of this study is that the difference between the tenure goal of "freedom" and the tenure goal of "efficiency" arises from an imperfect interpretation of what the perfect free enterprise system indicates about the nature of the perfect lease.^{9/}

II. The Concept of the Perfect Lease

What does the competitive free enterprise system indicate about the nature of the perfect lease? It is possible that part of the confusion over the goals arises because this point has not been clearly analyzed.

The heart of the private free enterprise economy is the free competitive market. For greatest efficiency this market should be perfectly competitive. Perfection exists when buyers and sellers have complete freedom to buy and sell in the market unhampered by product differentiation, lack of knowledge, discriminatory practices, rules, charges or other limitations.

But a free market alone does not create a perfect free enterprise economy. Producers must have complete freedom of production and consumers complete freedom of consumption directed only by supply and demand or prices in the free market. Likewise landlords may offer land for lease under different arrangements as demand and supply may direct. However, if these agreements interfere with the freedom of people to produce, exchange and consume they are an imperfection of the free enterprise society.^{10/} Hence, any tenure agreement which interferes with the firm's freedom to produce is an imperfection in this theoretical free enterprise system. Theoretically, perfect tenure, then, would give the firm complete freedom of production. Ordinarily this freedom would result in economic efficiency but there is no requirement that economic efficiency must be the result. The free competitive market provides ample opportunity for producers to fail or to exist at less than maximum efficiency.

^{9/} A trenchant criticism of the methods of setting tenure goals has just been made by Carl M. Bogholt, "The Value Judgment and Land Tenure Research," Land Tenure Research Workshop, Farm Foundation, Chicago, 1956, p. 131-7.

^{10/} Heady assumed competition and private ownership of resources and allocation of resources by market prices but fails mention that the farmer has freedom to respond to market prices as he wishes. Perhaps in a perfect economy the "perfect farmer" would respond as a puppet to prices but this is not a necessary or a realistic assumption. See Heady, Economics of Agricultural Production and Resource Use, p. 589.

The owner of a freehold estate has the least restrictions placed on his use or enjoyment of the land. However, even the owner of a freehold is not entirely free to do what he wishes with the property. For example, the freehold estate is subject to taxes, zoning laws, and eminent domain. Under the latter the state may take the land for public purposes. But ordinarily these limitations do not interfere with the entrepreneur's freedom to respond to market demand and supply. To the extent that they do not interfere, the freehold estate or fee simple ownership provides nearly perfect tenure because it gives the operator a high degree of freedom of production. Hence, the warranty deed which conveys the freehold is the most nearly ideal or "perfect" deed.

With this background one can now ask, "what is a perfect lease?" Like the deed, the lease conveys an estate in land. The fundamental difference is that the deed conveys land for an indefinite period or "forever" while the lease conveys or transfers land rights for only a definite period (or term) after which it reverts to the "seller" or landlord. This difference makes it necessary to include in the lease some provisions to give the landlord security of rent and security of his reversionary estate. These provisions are not necessary in the deed because the land does not revert to the grantor or seller. These considerations suggest that the perfect lease may be defined as one which gives the tenant with complete freedom of production and gives the landlord complete security of rent and security of property. Complete freedom of production includes fixity or security of tenure, freedom of operations and freedom of improvements -- the three F's previously mentioned.

The concept of economic efficiency used by many tenure workers as a guide to more perfect leases is a general goal or end for the entire economic system. It applies to owner-operatorship and partnerships, for instance, as well as to leasing. It is true, of course, that the perfect lease should give the tenant the freedom to operate efficiently if he wants to be efficient. But in the private free enterprise economy it is an error to say that a perfect lease must result in efficiency; it must result in a maximum freedom to be either efficient or inefficient as the operator desires. Hence, economic efficiency is neither a necessary nor a sufficient guide to the creation of a perfect lease.

III. The Imperfection of Share Rent Leases

If a perfect lease provides the tenant with complete freedom of operation and the landlord with complete security of rent and property then the imperfection of share rent leases is rather obvious. Share rents do not give the landlord as much security of the amount of rent as do fixed cash or fixed produce rents or the various flexible rents that vary with factors such as prices or county average yields -- factors which neither the tenant nor the landlord can affect during the term of the lease. Because the landlord lacks security as to the amount of rent under the share lease, he often refuses to give the tenant either security

of tenure or complete freedom of production. That share tenants lack freedom of production and usually operate under a one-year lease has been noted in many of the general leasing bulletins and circulars distributed to landlords and tenants. However, the causal relationship often has not been emphasized.

Thus, the imperfection of the share lease is found in the fact that the landlord's rent is subject to the control of the tenant. One argument often used in defense of share rents is that they protect the tenant against price, weather, insect, and disease risks which he cannot stand without the aid of the landlord. Few would argue that the purpose of the share rent lease is to protect the tenant against his own mismanagement.

When the share rent lease is defined as one in which a percentage of the crops raised on the leased land is paid as rent there seems to be no way of removing the tenant's control over the rent. However, if the share rent lease is defined more broadly as one in which the rent varies with yields and prices then improvement can be made. What is required is that a base rent be made to vary with crop yields and prices in a manner that cannot be affected by the tenant's management or honesty.

The nearest approach to the perfect share rent lease that is available at present is a base rent, in cash or produce, which varies with crop prices and county average yields. Such a lease is now being distributed in South Dakota.^{11/} Technically this lease is somewhat awkward since county yield data is not available until March of the next year. This necessitates a temporary settlement based upon the landlord's estimate of the county average yield. Also its usefulness is limited in some states because county average yields are not prepared.

IV. Perfect Lease or Perfect Partnership?

The imperfection of the share rent leases, then, is the fact that the landlord lacks security of rent since the amount of rent to be paid depends to an important extent upon the tenant's managerial ability and honesty in dividing the produce. It is important to note that this imperfection arises because the landlord and tenant have agreed to share the product according to their contributions to the lease as partners might share the product.

Thus an element of partnership is introduced into the lease. Because sharing the product affects very greatly the landlord-tenant relationship one might argue that this partnership element is more important than is the leasing element. In that case one might further argue that the thing to do is to perfect the partnership element in the share rent lease. This is apparently what Heady has done in an effort to create the perfect lease. His statement (quoted above) that a perfect leasing system must result in efficiency might just as well have been made regarding a perfect partnership.

^{11/} For further discussion of this rental arrangement see R. L. Berry, An Improved Farm Rental Method of South Dakota, South Dakota Agricultural Experiment Station Circular 141, 1958.

Furthermore, Heady's four rules for creating a perfect lease lend support to the idea that he is primarily concerned with perfecting the partnership aspect of the lease.^{12/}

If the words "partner" or "partnership" is substituted for the words "tenant" or "lease" in his rules they can be used as guides to create what might be called a "perfect partnership." In fact Heady has recognized that, in the long-run where the resources of both the landlord and tenant are variables, perfection can be brought about only if both parties own some of each category of resource, the proportion depending upon the share of the product to be received by either. "Thus, perfect share leases would almost always require complete partnership arrangements."^{13/}

When a perfect lease is defined as providing complete freedom of production the landlord has a role similar to a mortgage holder or a bondholder. He has security of income and property and he is not involved in the management of the firm. The weakness of the share rent is that it permits the landlord to enter the firm and take charge of the production without responsibility for the costs of production. Heady's rule that the landlord should share costs as the product is shared corrects this situation. However, the correction is achieved by making the landlord co-manager if not general manager of the firm. Thus, while efficiency maybe gained, the tenant's freedom of production is reduced. The share landlord uses a short term lease to insure control of the tenant's farming or at least to protect himself against possible mismanagement or dishonesty on the part of the tenant. The consequence of this action will be discussed in Section VII. below.

V. From Imperfect Lease to Imperfect Partnership

Perhaps the most serious objection to sharing costs as the product is shared is that it tends to transform an imperfect lease into an imperfect partnership and as a result compounds the possible sources of misunderstanding and friction.

Economists have been warned that mixing these relationship causes much confusion and uncertainty because of the rights, and the duties, and the liabilities of the parties differ under these relationships. In discussing father-son farming arrangements, Coe declares, "Under strict hiring arrangement the employer-father would be entitled to make all management decisions while under a strict lease the tenant-son would have

^{12/} Heady, Marginal Productivity of Resources, p. 601-2.

^{13/} Heady, Economics of Agricultural Production p. 601.

that right." In contrast, "The partnership contract can provide for any management arrangement desired." If there is no agreement the rights of partners to manage are equal under the Uniform Partnership Act.^{14/}

Leaving aside the strictly legal consequences of mixing the relationships of tenancy and partners there remains the moral and ethical questions which plague the landowner and the operator. Should the operator treat the landlord as a partner or as a landlord? Or, are there times when he can be considered the landowner and times when he should be considered as a partner? The landowner as a partner in the firm and as a landlord to the firm has much more power than an equal in the usual partnership. What should be his day-to-day role with respect to the tenant? When does he wear the hat of a landlord and when that of a partner? The confusion and the conflict between the landowner and the operator may never reach a court of law, but there can be little question that the confusion of roles must be expensive not only from the standpoint of economic efficiency but social well-being. A reasonable hypothesis for further study might be that sharing costs as the product is shared will yield a net loss rather than a net gain in social and economic efficiency.

VI. Are the Tenant's Costs Variable or Fixed?

A second objective to Heady's solution can be made. The desirability of sharing costs as the product is shared rests on the notion that the typical share tenant has the freedom to vary his inputs independently of the landlord. This notion apparently arises from the usual classification of farm costs as either fixed or variable and failure to recognize that what are variable costs for an owner operator may be fixed costs for a tenant.

Ordinarily land charges, depreciation of machinery and the operator's labor are generally regarded as fixed costs. All other costs such as fuel, oil, grease, repairs, seed, fertilizer, and weed and insect sprays are regarded as variable costs. But is this a realistic classification of these costs under a share rent lease? When the landlord rents a farm on a share basis he may say, "Now don't worry about keeping the farm, you can have it as long as you do a good job of farming and pay an honest share of the crop as rent." Even when he does not say anything about the quality of farming this is usually implied and understood. If the share lease is written the tenant is almost always required to farm in a business-like way or according to the rules of good husbandry.

It is generally recognized that such a lease makes the tenant's labor a fixed cost. Most landlords would object to their tenant taking a full or part-time job in town. Many object to the tenant leasing additional land or doing custom work on other farms. Some leases strictly forbid such activity. When this is the case, the tenant's labor and management may be considered as fixed by his lease contract in the same way that the labor of a hired man is fixed by a one-year contract.

^{14/} Edward J. Coe, "Legal Relationship Created by Father-Son Agreement," "Wisconsin Law Review, March 1950 (reprint), p 324.

If it is true that the tenant's unpaid labor is a fixed cost -- fixed by the lease contract -- are not other costs also fixed? Does not the tenant's agreement to "do a good job of farming" fix to a very large extent not only his labor inputs but also fuel, oil, grease, repairs and seed? May it not also include the application of commercial fertilizers if the landlord makes it clear that this is part of a good job of farming to which the tenant must agree in order to get and keep the farm?

Often share rent leases require that the landlord be consulted about the farming practice. In others the tenant is required to farm "to the satisfaction" or "under the direction" or "to the complete satisfaction and under the direction and subject to the approval" of the landlord. Other leases attempt to spell out what is meant by a good job of farming. But whether the details are specified or not, the tenant is usually quite aware that he has a fixed obligation to farm in a manner pleasing to the landlord. The short-term lease makes it possible for the landlord to enforce the agreement.

No doubt some tenants have second thoughts about their bargain. Some may plow a little less deeply and spend less effort on the seedbed preparation than was agreed, and they may neglect to make a last cultivation if the marginal product does not seem to justify the additional cash cost and the labor. However, customary ways of doing things have a strong influence where the effect of various rates or amounts are not precisely known. Some tenants may "fudge" a bit on the agreed rate of fertilizer application since it is costly and can be adjusted easily, if not very accurately. The difficulty of setting the fertilizer gauges to apply precisely the amount agreed upon, provides a good excuse for applying less. The general uncertainty as to the optimum amount of inputs makes it even easier for the tenant to ease his conscience when he adjusts the agreed rate. Nonetheless there has to be substantial performance of the agreement to keep the landlord from seeking a new tenant. Of course if the landlord has a reputation for insisting upon what tenants regard as unreasonable conditions, his chances of getting a tenant who will keep his agreements may not be very great.

D. Gale Johnson has also discussed the possibilities of fixing the inputs by the lease agreement. He believes that this is more common in Europe than in the United States. However, he notes that exceptions may exist in wheat areas of the Great Plains and sharecropping of the South. Wheat farm requires only modest inputs and the unpredictable variations of weather are great. As a result the farmer tends to farm according to custom. Hence, he believes the landlord has reasonable assurance that the land is being farmed with appropriate intensity. In the South he states that the plantation owner achieves the same end by furnishing all of the necessary supplies and limiting the acreage. This forces the cropper to farm intensely in order to make a living. In the Corn Belt, Johnson believes that the tenant has more freedom to vary his inputs, hence he argues other controls such as the one-year or year-to-year lease must be used to insure efficiency.^{15/}

^{15/} Johnson, p. 118-23.

While it is undoubtedly true that the Corn Belt farmer has a wider range of inputs which can be made the requirement that he do a good job of farming seems to put a definite lower limit to this range. Perhaps an even more important limitation is custom and community pressure. The social status of a "sloppy farmer" or a "poor farmer" or a "land-hog" is not very high. He may be making more money but most of his neighbors will call him a failure if his crops do not measure up to the standards of the community. In any case there seems to be no reason why the costs of the Corn Belt tenant cannot be fixed to a considerable degree by the lease. To the extent that costs can be fixed there is no need for sharing costs as the product is shared.

These considerations suggest that the division of costs as the product is shared will probably be limited largely to fertilizer. Here it will be most useful when the rate of application is heavier than the accepted rate in the community. It is also useful in preserving existing rental shares when fertilizer or some other such input is first introduced on a rented farm.

VII. Freedom of Production and Improvement

As has been shown a perfect lease would give the tenant complete freedom of production and landlord complete security of rent and property. If the tenant's freedom of production is to be equal to that of an owner operator then the tenant must have a comparable feeling of security of tenure so that he can make plans for crops and livestock over several years time. Long-run plans also frequently require improvements in cropland, pasture, fences and building. Short-run or yearly plans may also call for improvement but these are a less serious problem. In the short run, landlords are compelled to furnish the minimum of improvement necessary for operation in order to obtain a tenant.

The insecure tenant with a short-run planning horizon is not likely to be interested in long run improvement on the farm. Hence, security of tenure seems to be of fundamental importance if the tenant is to have the freedom of production comparable to that of an owner operator. Heady has recognized the importance of security of tenure in his rules to achieve efficiency or the perfect lease. His proposal is that the tenant be given either a long-term lease or compensation for the unexhausted value of his improvements.^{16/} These proposals will now be examined.

Is Heady's proposal that the landlord give the tenant security of tenure by a long term lease realistic in view of the fact that under a share rent the landlord has less security as to the amount of rent than do fixed rent landlords? Is his proposal consistent with his Rule 1 which would require the landlord to share not only the product but the costs of production?

^{16/} Heady, Marginal Productivity of Resources, p. 602. See also his Economics of Agricultural Production, p. 614-16

Serious objections can be raised to the long-term lease as a solution. D. Gale Johnson has argued that landlords must use a short term lease to insure efficiency and adequate rents under the crop share lease.^{17/} Farm landlords seem to agree. For example when South Dakota landlords were asked why one-year leases are customarily used, 65 percent of the 234 landlords answering this question checked the following statement: "Because the short term lease keeps the tenant on his toes since he knows that you can get another tenant if he does a poor job."^{18/} These replies suggest that landlords believe that a one-year or a year-to-year lease is necessary to provide them with security of rent and property under the share rent lease which 90 percent of them are using.

Wallace and Beneke also argue that the short-term lease should be used. They say that while the tenant may press for an unqualified three-or five-year lease, it deprives the landlord of his only recourse in the event the tenant is not performing satisfactorily -- a change in tenants. They hold a long term lease " . . . dulls the incentive of the tenant to do his best work by giving him a false sense of security."^{19/}

The evidence presented above suggests that the short term lease is necessary to insure that a good job of farming will be done and will continue to be insisted upon by landlord as a means of insuring that they receive a fair rent.

Would landlords who insist upon a short-term lease be willing to enter an agreement to compensate their tenants for the unexhausted value of any improvement they might make? No doubt many examples can be found where landlords have made such agreements. For some tenants who feel quite secure even though they have a one-year or year-to-year lease this may be quite satisfactory. But the tenants who do not feel secure, such a promise is likely to have little appeal. They are not likely to want to make improvement unless they are going to be around to enjoy them. The

^{17/} Johnson, p. 119-20.

^{18/} The other alternatives were (1) "Because the long term leases are not as binding on tenants as they are on landlords" (2) "Because the one-year lease gives the landlord a chance to increase his rent as expenses rise" and (3) "other". See R. L. Berry, Share Rents and Short Term Farm Leases, South Dakota Agricultural Experiment Station Circular 117, 1955, p. 9-13, Table 7.

^{19/} J. J. Wallace and R. R. Beneke, Managing the Tenant Operated Farm, Iowa State College Press, Ames, 1956, p. 62.

insecure tenant usually has more attractive alternatives for his limited funds than investing it in real estate of his landlord. Because of these factors there is danger in suggesting that either long-term leases or compensation for unexhausted improvements will result in a perfect share rent. Long term leases are not the only way that a tenant acquires a sense of security necessary for freedom of production and therefore improvement. Compensation is not a substitute for a feeling of security except possibly when the compensation provisions are unusually generous, and hence not likely to be made.

VIII. Conditions Required to Create A Perfect Lease

The perfect lease has been redefined as one which gives the tenant complete freedom of production and the landlord complete security of his rent and property. As compared to cash leases, the share rent lease is less perfect because of the share tenant's control over the amount of the rent to be paid in any given year. If this is the imperfection of share rent leases there seems to be little prospect that Heady's rule that costs should be shared as the product is shared can eliminate it. Nonetheless, the listing of the conditions which are necessary for a perfect lease has some merit. Hence two sets of conditions or "rules", one set for the landlord and one set for the tenant, are presented below.

The three rules which, if followed, would give the landlord security of rent and property are as follows:

1. The landlord should have security as to the amount of his rent. As has been shown this requires an objectively determined rent. A share or percentage rental arrangement in which the rent can be affected by the tenant and to some extent by the landlord does not satisfy this rule.

2. The landlord should have security as to the payment of his rent. Some kind of lien or guarantee is necessary here. What is needed is something similar to the guaranteed mortgage loans of the Farmer's Home Administration.

3. The landlord should have compensation for damages committed or permitted by the tenant. Most leases and much of the law seem inadequate to achieve this goal. For example, in most states, if the tenant commits or permits waste the landlord can collect triple damages but such an unreasonable penalty cannot be enforced by jury trial in most communities.

These three rules are clearly implied in the definition of the perfect lease, these ideas are not new, they are long-recognized problems of leasing which have been discussed by tenure workers for many years. Farm tenure workers need to get on with this task. The landlords are not likely to provide freedom and security for their tenants until their rent and property is secure.

Landlords, in an attempt to protect their rent or property may specify rental conditions which violate unnecessarily the tenant's freedom of production. To prevent this the following conditions or rules are suggested:

1. The tenant should receive all the product and pay all the expenses (including a rent for the land). This rule makes the tenant the manager of an independent firm which has purchased the use of land for a definite period much as a manufacturer might lease a building in which to conduct his business. In other words when a rent is a share or percentage of the product of the land leased a perfect lease is not possible.

2. The rental rates charges per acre should be uniform regardless of the crop or livestock to be produced on a given quality of land. If the rates vary with crops and livestock produced, they are discriminatory and hence they limit the tenant's freedom of choice of crops and livestock. For example, if the landlord charges \$10 per acre for land of a given grade when it is used for corn and \$5 per acre when it is used for oats, the tenant will tend to produce more oats than he would if he paid a uniform rate for the land regardless of the crop grown. Thus, discriminatory rental rates rather than market prices tend to determine the tenant's production plans.

3. A specific rental rate should be charged for each kind of resource furnished. Not only must the landlord have the security of rent provided by a fixed or an objectively determinable total rent, but the amount of rent which he receives from each kind of resource leased also must be fixed or objectively determinable. Unless the landlord knows definitely what he is receiving for the house, barns, and pastures, as well as for cropland, he has no basis for decisions as to whether or not he should maintain or improve them. Hence the tenant's freedom of production will be limited by this uncertainty. A recent survey has shown that tenants regard the upkeep of improvement as the most important cause of landlord-tenant disagreement.^{20/} While this source of difficulty probably will not be entirely removed by more definite or specific rentals, it seems that it should be decreased.

4. The improvement of the farm should be encouraged. The farm must be of adequate size if it is to be efficient. This may mean that the perfect lease should not deny the tenant freedom to operate other land provided he is willing to bear the risks involved. Measures which not only conserve but improve the land may be needed. The house, barns, fences, water systems, and electric systems usually need to be improved from time to time. Hence the lease should provide that such improvements can be made either: (a) at the landlord's expense with an appropriate increase in rent, or (b) at the tenant's expense. If the latter, the tenant's expense should be offset either by compensation for the unexhausted value of the improvements when he leaves the farm or by

^{20/} R. L. Berry and Vernon E. Bau, Tenant Interest in Cash and Flexible Cash Leases in Moody County, South Dakota Agricultural Experiment Station Bulletin 480, 1959. Table 7.

permission to remove (or sell) the improvements! This rule is closely related to the fact that a perfect lease requires that the landlord be compensated for damages by the tenant. It seems only reasonable that the landlord compensate the tenant for improvements or permit him to remove or sell them to others.

5. The tenant should be given security of tenure. Security of tenure is necessary if the tenant is to have freedom of production comparable to that of the owner-operator. Without security of tenure it is difficult to make long-range crop and livestock production plans. Insecure tenure dampens, if not destroys, the tenant's interest in maintaining and especially improving the soil and buildings on the farm. Such security of tenure can be provided by other means than a long term lease. A permanent professional landlord using a 1-year cash lease with many tenants has apparently given the Scully tenants a high degree of security and freedom. The fact that the tenants own the improvements may also be a factor. However, owner-operators, share tenants and the Scully tenants did not believe ownership was nearly as important as the cash rental and the size of the estate as factors affecting the Scully tenants' security and freedom.^{21/}

When these five rules to protect the tenant's freedom of production are compared with Heady's four rules it can be seen that they are somewhat similar. Heady's rule 1 for share rent leases requires that costs be shared as the product is shared. In the new rule the landlord's share of the product would be zero and hence his share of the costs should also be zero. There is no fundamental difference between Heady's rule that the shares of all competitive crops must be the same or equal and the new rule 2 that rental rates should be uniform regardless of the crop or livestock to be produced on a given quality of land. Heady's rule 3 that the landlord must have a specific rent for each class of improvements which he furnishes is repeated in new rule 3. Finally, Heady's rule 4 that the tenant must have security of tenure or compensation for unexhausted improvements is presented as new rules 4 and 5. Unless the tenant is secure he is not apt to make improvements for which he should be compensated. Aside from rule 1 the most important difference between these new rules and Heady's is that they have been broadened to cover all leasing arrangements.

IX. Summary and Conclusions

Historically, freedom of production appears to have been the goal of farmers seeking to improve farm tenure. If this goal is rational then it seems that it should also be consistent with the private free enterprise system in which it is found. Yet when an effort was made to deduce the goals from the free enterprise system, efficiency rather than freedom seemed to be the goal.

^{21/} An unpublished study of the Scully Estate, Economics Department, South Dakota Agricultural Experiment Station, 1955.

The main purpose of this article was to reconcile these goals by developing a more refined concept of the perfect lease and some new rules to achieve it. The analysis indicates that a perfect lease would give the tenant complete freedom to produce what the market demands and the landlord security of rent and property. Since security of tenure is necessary for freedom of production, this is also implied. As compared to a cash rent lease, the share rent lease is less perfect because the tenant, and to some extent the landlord, can affect the amount of rent to be paid during the lease year.

Because the share rent landlord lacks security as to the amount of his rent he must limit the tenant's freedom of operation either directly by lease provisions or indirectly by the use of a short-term lease. The short-term lease permits the landlord to remove the tenant if he does a poor job of farming or fails to pay a fair rent. The lease nearest to the share rent lease is a flexible or sliding scale lease in which the base rent varies with both crop prices and county average yields.

While the sharing of costs as the product is shared makes it possible for the share tenant to farm as intensely as an owner-operator or a cash tenant, it does not remove the landlord's insecurity as to the amount of the rent. Rather than become involved with the tenant as a partner as well as a landlord the wiser course would seem to be to fix the "variable" costs by the lease agreement in the same way that the tenant's labor is fixed and continue to use the short-term lease to secure compliance until landlords and tenants become willing to adopt a more perfect lease by using fixed cash, fixed produce (standing rent), or other objectively determined rents such as those which vary a base rent by crop prices and county average yields.

Three rules seem necessary to protect the landlord's rent and property. These are (1) only fixed cash, fixed produce, or other objectively determinable rents shall be used, (2) the payment of the rent shall be guaranteed by some kind of lien, and (3) the productivity of the landlord's property must be guaranteed by reasonable safeguards and penalties.

In an effort to achieve security of rent and property the landlord may (1) share costs, (2) use discriminatory rents, (3) fail to agree upon a rent for each kind of resource furnished, (4) limit the tenant's security of tenure, and (5) fail to make compensation for improvements. All of these five actions appear to limit the tenant's freedom much more than they increase the landlord's security of property. Hence, rules are made against such action. Except for the first, these are similar but broader than the rules now being used by some economists in the land tenure field.